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Supreme Court of the United States

October Term, 1948

No.....

ED THYS and ALBERT K. MILLER, co-partners doing business as THYS & MILLER,

Petitioners,

vs.

THE STATE OF WASHINGTON,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF WASHINGTON AND BRIEF IN SUPPORT OF PETITION

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Supreme Court of the United States

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No.....

ED THYS and ALBERT K. MILLER, co-partners doing business as THYS & MILLER,

Petitioners,

vs.

THE STATE OF WASHINGTON,

Respondent.

TO THE HONORABLE CHIEF JUSTICE AND ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

The petitioners, Ed. Thys and Albert K. Miller, co-ners doing business as Thys & Miller, pray that a of certiorari issue to review the judgment of the reme Court of the State of Washington entered in the ve entitled cause on December 13, 1948 (R. 138-9), tion for rehearing denied December 13, 1948 (R. 138), ersing the judgment of the Superior Court of the State Vashington for Thurston County. (R. 79).

STATEMENT OF THE CASE

The primary issue in this proceeding is the question he legality and constitutionality of state sales taxes business and occupation taxes imposed by respondent,

the State of Washington, upon petitioners, Thys & Miller, in certain interstate commerce transactions involving patent royalties on hop picking machines.

Petitioners as plaintiffs filed in the Superior Court of Thurston County, Washington, two notices of appeal and complaints, later consolidated for all purposes, contesting the legality and constitutionality of two tax assessments for the years 1941 through 1944, both inclusive, and certain orders and decisions of the Tax Commission of the State of Washington. Petitioners paid under protest the two assessments, $3,080.37 and $11,772.43 respectively, and sued for refund and for an adjudication of illegality. (R. 65-73). Much larger amounts for future years are indirectly involved.

After a non-jury trial, the court entered judgment in favor of petitioners. (R. 79-81). Upon appeal by the State, the State Supreme Court reversed, and held that the taxes in question were lawfully assessed, three judges vigorously dissenting. (R. 103-138).

The material portions of the state tax statute, namely, Titles II and III of the Revenue Act of 1935 (chap. 180) as amended (Remington's Revised Statutes of Washington, sec. 8370-4 to 8370-25, and 8370-199, as amended) are quoted in the appendix to our brief.

The facts are for the most part substantially undisputed and may be briefly summarized as follows:

Petitioners, Thys & Miller, have, at all times material, resided at Sacramento, California, and have their sole office and manufacturing plant there. They have never had a place of business anywhere else. They have never had an office nor place of business of any nature whatever, nor any stock of merchandise, nor any authorized agent or employee in the State of Washington. (R. 16, 17, 20, 37, 44-5, 85, 89, 93, 95).

Petitioner, Ed. Thys, is an inventor. As a result of a tremendous amount of labor and research performed in California, he has invented and obtained U. S. patents on numerous improvements in hop picking machines. (R. 20, 31).

Due partially to the acute labor shortage caused by the war, a considerable number of hop picking machines containing petitioner's patented improvements have been used by hop growers in the State of Washington during the past several years.

Accordingly, petitioners in California entered into a written contract with Lindeman Power Equipment Company, a corporation, of Yakima, Washington, for the manufacture of these machines. Petitioners made occasional inspection trips to Yakima, but reserved no right of con-

trol and exercised no control whatever over the operation of the Lindeman plant or the manufacture of the machines. No Lindeman representative ever had any authority to sign any contract for petitioners. (R. 30, 34, 43-4, 93). The relationship was clearly that of independent contractors. (R. 20-1, 30, 34-5, 43-6, 49, 89, 91-2; Pltf. Ex. 9).

No sales solicitation was necessary and none was made for the reason that Yakima hop growers quickly became familiar with Thys machines, and their demand therefor at all times greatly exceeded the available supply thereof. This again was caused partially by the acute shortage of both labor and materials due to the war. (R. 32-3, 92, 95-6, 99, 100, 102).

Petitioners in California entered into a written contract, dual in nature, with each machine purchaser. Each contract provided: (1) for the sale of the picking machine from petitioners to the purchaser for a certain stated purchase price (varying through the years from $5,000.00 to $6,350.00—which included the cost of manufacture plus a profit margin).

Each contract also provided: (2) that petitioners granted a license to the purchaser to use any or all of petitioners' inventions, listing the patents thereon, in consideration of which the purchaser agreed to pay petitioners an annual royalty for a period of 17 years at rates varying

from $5.00 to later $3.00 per 200 pound bale of hops picked with the machine. (R. 20-1, 44, 86, 93; Pltf. Ex. 8).

Paragraph 6 of the contract (Pltf. Ex. 8; petitioners being first party and the purchaser, second party) reads in part as follows:

> "It is expressly understood that the sale of said machines is without the right to use said machines, and that in order to use said machines Second Party must secure from First Party a license to use said machines, and that the continuing right to use said machines is strictly conditioned upon the full and faithful performance of such license; wherefore, First Party hereby grants to Second Party a non-exclusive, indivisible and non-transferable license, as long as the terms hereof be fully and faithfully performed and maintained, to use said machines, for the purpose for which said machines were designed, under the following United States Letters Patent: . . . ,"

followed by a description of the patents pursuant to which the machine was made and sold.

By paragraph 7, petitioners granted to the purchaser,

> ". . . strictly subject to the full and faithful performance of the terms and all thereof of this agreement, a non-exclusive, indivisible and non-transferable license to use and enjoy, in connection with hop picking and separating operations of Second Party, the methods and processes disclosed and claimed in United States Letters Patent (describing the patents)."

Paragraph 8 of the contract reads, in part, as follows:

> "For and in consideration of the licenses and each there-

of, set forth in Paragraphs VI and VII hereinabove, Second Party agrees to pay to First Party a royalty of Five Dollars ($5) per two hundred (200) pounds of dried hops harvested by machines purchased by Second Party, said royalty being payable when the amount of bales picked is determined or on or before the 15th day of October of each year during the term hereof, for all hops harvested during the preceding twelve (12) calendar months. In any event, the minimum royalty payable hereunder shall be Five Hundred Dollars ($500) per machine per annum, and if the royalties computed at the rate of Five Dollars ($5) per two hundred (200) pounds of hops harvested shall not aggregate as much as Five Hundred Dollars ($500) for each machine in each period of twelve (12) months herein referred to, said sum of Five Hundred Dollars ($500) per machine shall nevertheless be paid to First Party by the following October 15th."

In all cases the purchase price was fully paid and title to the machine passed to the purchaser either prior to or at the time of delivery of the machine, and each contract so provided. (R. 21-3, 44; Pltf. Ex. 8).

There is no evidence whatever impugning in any manner the good faith of petitioners, nor showing any fraudulent intent to evade, nor indicating that these contracts were anything but what they purported to be. On the contrary the evidence establishes petitioners' entire good faith in these transactions. (R. 23).

It is undisputed that the business and occupation tax for manufacturing and the sales tax for the purchase price of the machines, whether actually taxable or not, have been

fully paid. The sole controversy relates to the taxability of the patent royalties under title II, the ¼% occupation tax, and title III, the 3% sales tax. (R. 9, 21-2, 23-4, 39, 41, 48, 93-4).

These were bona fide patent royalties and were never intended as part of the selling price of the machines. (R. 21, 23, 44, 98).

Petitioners shipped from their plant in Sacramento, California, to Lindeman at Yakima, Washington, huge quantities of parts which became component parts (more than 15%) of the completed machines. (R. 14-6, 29, 33, 36-7, 39-42, 47, 88, 91-2).

JURISDICTIONAL STATEMENT

This Court has jurisdiction to review the judgment here in question by writ of certiorari, pursuant to title 28, U. S. Code, sec. 1257, and particularly paragraph (3). As construed and applied herein by the state supreme court the state tax statute in question is invalid, unlawful, and unconstitutional because repugnant to the Commerce Clause of the Constitution (Art. I, sec. 8, clause 3) and the Due Process Clause of the Fourteenth Amendment, and also the Patent Clause of the Constitution (Art. I, sec. 8, clause 8), and the federal patent statutes.

Also and in any event, the rights, privileges and im-

munities of the petitioners claimed under the said three constitutional provisions and laws are violated by the said state supreme court decision and judgment.

The judgment of the state supreme court to be reviewed was entered on December 13, 1948, and order denying our petition for rehearing was entered on the same date. (R. 138, 139). Pursuant to title 28, U. S. Code, sec. 2101, par. (c), an order was entered on February 28, 1949, by one of the Associate Justices of this Court extending the time for filing this petition for writ of certiorari to and including April 12, 1949. (R. 141).

The jurisdiction of this Court is also invoked under paragraph 5 (a) of Rule 38 of this Court.

QUESTIONS PRESENTED

The principal questions presented herein are:

1. Where petitioners in California sold patented hop picking machines to residents of the state of Washington, and in California executed written license contracts providing for the annual payment to petitioners of certain patent royalties for the use thereof, can the State of Washington lawfully tax such royalties without infringing the Commerce Clause of the Federal Constitution?

2. Are such patent royalties income from intangible

property which is legally taxable only in the state of the domicile of the patent holders under the law and the Due Process Clause of the Fourteenth Amendment of the Constitution?

3. Where patented hop picking machines were sold and the full agreed purchase price paid and title thereto passed to the purchasers pursuant to written contracts, which also provided that the seller granted a license to the purchaser for the use thereof, and in consideration thereof the purchaser agreed to pay an annual royalty for such use over a period of years according to the quantity of hops picked with such machine, and the contracts were made in good faith without fraudulent intent to evade, do such royalties constitute part of the selling price so as to be taxable under a state sales tax measured by 3% of the selling price?

4. Where the patentee partners resided and had their sole office and place of business in California, and no office, place of business or authorized agent in Washington, and all contracts for the sale and licensing of patented hop picking machines to residents of Washington were always entered into by the sellers solely in California, and due to war conditions during the years in question there was no solicitation of sales in Washington and none necessary, as the demand greatly exceeded the available supply, were

said patentees doing business in Washington so as to be subject to a local sales tax on such interstate commerce transactions?

REASONS FOR ALLOWANCE OF WRIT

The following reasons are relied on by the petitioners for the allowance of the writ of certiorari herein, pursuant to paragraph 5 (a) of Rule 38 of this Court:

1. That the state court of last resort has decided federal questions of substance, which, unless the decisions hereinafter cited are deemed controlling, have not been heretofore directly determined by this Court.

Each of the four questions presented, hereinabove mentioned, is, we submit, a federal question of substance. Each of them is of substantial public importance. So far as we are aware, this Court has never previously directly determined any of the foregoing questions, and particularly the first three questions hereinabove mentioned. These questions are of sufficient public importance that they should now be directly determined by this Court herein.

State taxation of royalties received from federal patents, and state taxation of interstate commerce transactions, especially outside of the state of the taxpayer's domicile, as well as the question whether under these circumstances petitioners were doing business in the State of

Washington—each of these is, we submit, a federal question of substance and of substantial public importance in the administration of the law under our dual federal system of government.

This is undoubtedly correct as to each and all of the four questions presented, hereinabove mentioned, unless it be considered that the decisions of this Court hereinafter cited in our brief are controlling and decisive of these questions in favor of petitioners.

2. The state court of last resort has also (and we do not conceive this to be inconsistent) decided the said federal questions of substance in a way not in accord with applicable decisions of this Court, including the following cases:

Freeman v. Hewit, 329 U. S. 249, 91 L. Ed. 265; *McLeod v. Dilworth Co.*, 322 U. S. 327, 88 L. Ed. 1304; *Joseph v. Carter & W. Stevedoring Co.*, 330 U. S. 422, 91 L. Ed. 993; *Nippert v. Richmond*, 327 U. S. 416, 90 L. Ed. 760; *Fisher's Blend Station v. Tax Commission*, 297 U. S. 650, 80 L. Ed. 956; *Puget Sound Stevedoring Co. v. State Tax Commission*, 302 U. S. 90, 82 L. Ed. 68; *Gwinn, White & Prince v. Henneford*, 305 U. S. 434, 83 L. Ed. 272; *Adams Mfg. Co. v. Storen*, 304 U. S. 307, 82 L. Ed. 1365; *First National Bank v. Maine*, 284 U. S. 312, 76 L.Ed. 313; *People's Tobacco Co. v. American Tobacco Co.*, 246 U. S. 79, 62 L. Ed. 587; *Central Grey-*

hound Lines v. Mealey, 334 U. S. 653, 92 L. Ed. (Adv. Op.) 1235.

3. The state court of last resort has decided federal questions of substance in a way untenable, in conflict with the weight of authority, and contrary to the decisions of other courts, including the following cases:

Newport Co. v. Wisconsin Tax Commission, 219 Wis. 293, 261 N. W. 884, 100 A. L. R. 1204, cert. denied, 297 U. S. 720, 80 L. Ed. 1004; *State ex rel Cruse v. American Can Co.*, 117 Colo. 312, 186 P. 2d 779; *Standard Oil Co. v. Johnson*, 33 Cal. App. 2d 430, 92 P. 2d 470.

In the Newport case, the supreme court of Wiscossin reached a different conclusion from the Washington court and held that income from patents can be taxed only in the state of the patentee's domicile without infringing the Due Process Clause of the Constitution. This decision was approved by this Court by denial of certiorari.

4. The Washington Revenue Act of 1935 as amended, Laws of 1935, Ch. 180, Laws of 1939, Ch. 225, and Laws of 1941, Ch. 178, is unconstitutional, especially as applied to the petitioners, and repugnant to both the Commerce Clause and the Due Process Clause of the Constitution. The decision of the state supreme court was in favor of the validity of said state statute.

5. For the reason last hereinabove mentioned, the petitioners would have a right of appeal to this Court pursuant to title 28, U. S. Code, sec. 1257, par. (2). However, it seems to the petitioners preferable to come to this Court by certiorari in the belief that not only said two constitutional questions, but all four of the questions herein presented, as hereinabove stated, may be authoritatively and directly determined by this Court.

Wherefore, your petitioners pray that a writ of certiorari issue under the seal of this court directed to the Supreme Court of the State of Washington commanding said court to certify and send to this Court a full and complete transcript of the record and of the proceedings of the said state supreme court had in the case numbered and entitled on its docket No. 30281, Ed Thys and Albert K. Miller, co-partners doing business as Thys & Miller, respondents, vs. State of Washington, appellant, to the end that this cause may be reviewed and determined by this Court as provided for by the statutes of the United States; and that the judgment herein of said state supreme court be reversed by this honorable Court, and that your petitioners may have such other and further relief in the premises as to this Court may seem proper.

ELWOOD HUTCHESON
GEORGE W. WILKINS
Attorneys for Petitioners

Supreme Court of the United States

October Term, 1948

No.....

ED THYS and ALBERT K. MILLER, co-partners doing business as THYS & MILLER,

Petitioners,

vs.

THE STATE OF WASHINGTON,

Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

OPINION OF THE COURT BELOW

The opinion of the state supreme court is reported in 131 Wash. Dec. 689, 199 P. 2d 68; petition for rehearing denied, 132 Wash. Dec. 101. (R. 103-138).

JURISDICTION

The Court has jurisdiction to review the judgment here in question by writ of certiorari, pursuant to title 28, U. S. Code, sec. 1257, and particularly paragraph (3). As construed and applied herein by the state supreme court the state tax statute in question is invalid, unlawful, and

unconstitutional because repugnant to the Commerce Clause of the Constitution (Art. I, sec. 8, clause 3), and the Due Process Clause of the Fourteenth Amendment, and also the Patent Clause of the Constitution (Art. I, sec. 8, clause 8), and the federal patent statutes.

Also and in any event, the rights, privileges and immunities of the petitioners claimed under the said three constitutional provisions and laws are violated by the said state supreme court decision and judgment.

The judgment of the state supreme court to be reviewed was entered on December 13, 1948, and order denying our petition for rehearing was entered on the same date. (R. 138, 139). Pursuant to title 28, U. S. Code, sec. 2101, par. (c), an order was entered on February 28, 1949, by one of the Associate Justices of this Court extending the time for filing this petition for writ of certiorari to and including April 12, 1949. (R. 141).

The jurisdiction of this Court is also invoked under paragraph 5 (a) of Rule 38 of this Court.

The four questions presented, enumerated in the foregoing petition for certiorari, have been at all times directly raised by the petitioners in each of the said courts. Each of these questions was directly raised in each of the two notices of appeal and complaints filed by the petitioners at the inception of this proceeding. (R. 3, 4, 66, 67, 70-2).

The state supreme court decision shows that all of these questions, including the constitutional questions, were at all times directly raised and vigorously contended for by the petitioners. (R. 111, 112).

We therefore submit that the nature of the case and of the rulings in the court below were such as to bring this case directly within the said statutory jurisdictional provisions.

The cases believed to sustain such jurisdiction are as follows:

Charleston Fed. Sav. & Loan Assn. v. Alderson, 324 U. S. 182, 187; 89 L. Ed. 857, 862; *Brooklyn Savings Bank v. O'Neil*, 324 U. S. 697, 701, 89 L. Ed. 1296, 1306; *Joseph v. Carter & W. Stevedoring Co.*, 330 U. S. 422, 91 L. Ed. 993; *Citizens National Bank v. Durr*, 257 U. S. 99, 66 L. Ed. 149; *Ex Parte Williams*, 277 U. S. 267, 72 L. Ed. 877; *Ireland v. Woods*, 246 U. S. 323, 328, 62 L. Ed. 745, 749; *Fullerton v. Northern P. R. Co.*, 266 U. S. 435, 69 L. Ed. 367.

Federal questions of substance are presented.

American Sugar Ref. Co., v. Louisiana, 179 U. S. 89, 45 L. Ed. 102; *Tregea v. Modesto Irrigation Dist.*, 164 U. S. 179, 41 L. Ed. 395; *Bell's Gap R. Co. v. Pennsylvania*, 134 U. S. 232, 33 L. Ed. 892; *Illinois C. R. Co. v. Chicago*, 176 U. S. 646, 44 L. Ed. 622.

STATEMENT OF THE CASE

This has already been stated in the preceding petition, and the same is hereby adopted, incorporated by reference herein, and made a part of this brief.

SPECIFICATION OF ERRORS

1. The state supreme court erred in holding that the State of Washington may lawfully tax petitioners' patent royalties on hop picking machines sold to residents of Washington by the petitioners in California without infringing the Commerce Clause of the Constitution.

2. The state supreme court erred in holding that such patent royalties are not income from intangible property and are not legally taxable only in the state of the patent holders' domicile, under the Due Process Clause of the Constitution.

3. The state supreme court erred in holding that these patent royalties constitute part of the selling price of the hop picking machines, and are therefore taxable under the state sales tax, and business and occupation tax, measured by 3% and ¼% of the selling price, respectively.

4. The state supreme court erred in holding that the petitioners were and are doing business in the State of Washington, and therefore are subject to payment of state

sales taxes and business and occupation taxes in that state on these patent royalties.

5. The state supreme court erred in entering its judgment reversing the judgment of the superior court of Thurston County, Washington. (R. 138-9).

6. The state supreme court erred in denying our petition for rehearing. (R. 138).

7. The state supreme court erred in holdinv said state tax statute constitutional.

ARGUMENT

SUMMARY OF THE ARGUMENT

1. Where the petitioners in California sold patented hop picking machines to residents of the State of Washington, and in California executed written license contracts providing for the annual payment of certain royalties for the use thereof, the State of Washington may not lawfully tax such royalties without infringing the Commerce Clause of the Federal Constitution.

2. Such patent royalties are income from intangible property, and therefore are legally taxable only in the state of the patent-holder's domicile, under the Due Process Clause of the Fourteenth Amendment of the Constitution.

3. Where patented hop picking machines were sold

and the full agreed selling price was paid and the title passed to the purchasers pursuant to written contracts which also provided that the seller granted a license to the purchasers for the use thereof and in consideration thereof the purchasers agreed to pay an annual royalty for such use over a period of years according to the quantities of hops picked with such machine, and the contracts were made in good faith and without fraudulent intent to evade, such patent royalties do not constitute part of the selling price so as to be taxable under a state sales tax and business and occupation tax measured by 3% and ¼% respectively of the selling price.

4. Where the patentee partners resided and had their sole office and place of business in California and no office, place of business or authorized agent in Washington, and all contracts for the sale and licensing of patented hop picking machines to residents of Washington were always entered into by said sellers solely in California, and due to war conditions during the years in question there was no solicitation of sales in Washington, and none necessary, as the demand greatly exceeded the available supply, said patentees were not doing business in the State of Washington so as to be subject to a local sales tax or business tax on such interstate transactions.

1. THESE TAXES ARE AN ILLEGAL AND UNCONSTITUTIONAL IMPOSITION UPON INTERSTATE COMMERCE

Irrespective of whether these payments be deemed patent royalties, as we contend, or part of the selling price, we submit that the State of Washington by imposing this state sales tax and business tax thereon infringed the petitioners' constitutional rights under the .Commerce Clause (Art. I, sec. 8, clause 3) of the Federal Constitution. This tax is an unlawful burden which the state is attempting to impose upon interstate commerce transactions. Each of these dual sales and license-royalty contracts was in all instances executed by the petitioners at their sole office in Sacramento, California. (R. 20-1, 44, 86, 93). Each written contract was executed by the petitioners in California and crossed the state line and legally was as much a sale and license contract in interstate commerce as though the machines themselves were shipped across the state line.

Even though the completed machines themselves did not cross the state line, these were clearly interstate commerce transactions whereby *the petitioners in California sold these machines* to hop growers in Washington.

Moreover, substantial parts (over 15 %) of the machines were manufactured by petitioners at their Sacra-

mento plant and shipped from California to the Lindeman plant at Yakima, Washington, where they became component parts of the finished machines. (R. 14-6, 29, 33, 36-7, 39-42, 47, 88, 91-2). Thereafter said hop growers annually paid patent royalties thereon to petitioners, who received the same at their Sacramento, California, office. Manifestly, therefore, these were transactions in interstate commerce, the gross proceeds of which can be directly taxed only by Congress and not by the State of Washington.

This legal question is a federal question of substance, and unless the cases hereinafter cited are deemed controlling in favor of petitioners, has not heretofore been directly determined by this Court. It is a question of substantial public importance in the field of state taxation of interstate commerce transactions. It is a question which should be directly determined by this court.

Moreover we submit that the state supreme court decision is not in accord with applicable decisions of this Court.

In three previous cases this Court reversed the state supreme court of Washington and held that this same state tax statute is unconstitutional under the Commerce Clause. This should now be done for the fourth time in this case.

In *Fisher's Blend Station v. Tax Commission,* 297 U. S. 650, 80 L. Ed. 956, reversing 182 Wash. 163, 45 P. 2d 942,

49 P. 2d 1151, this Court held this same tax on a radio broadcasting station is unconstitutional under the Commerce Clause, and that sending "electro-magnetic waves" between states constitutes interstate commerce, even though all of the sounds of the radio programs were produced not by the station but by its customers, citing and following among other cases *Van Dusen v. Dept. of Labor and Industries*, 158 Wash. 414, 290 Pac. 803. Justice Stone, speaking for this Court, said:

> "In all essentials this procedure does not differ from that employed in sending telegraph or telephone messages across state lines, which is interstate commerce. (Citing cases.) . . . Whether the transmission is effected by the aid of wires, or through a perhaps less well understood medium, 'the ether,' is immaterial, in the light of those practical considerations which have dictated the conclusions that *the transmission of information interstate is a form of 'intercourse,' which is commerce. . . . As appellant's income is derived from interstate commerce, the tax, measured by appellant's gross income, is of a type which has long been held to be an unconstitutional burden on interstate commerce.*" (Citing cases). (All italics are ours).

In *Puget Sound Stevedoring Co. v. Tax Commission*, 302 U. S. 90, 82 L. Ed. 68, reversing 189 Wash. 131, 63 P. 2d 532, this Court made the same holding as to this tax on gross receipts of a stevedoring company engaged in locally loading and unloading cargos for interstate shipments. Justice Cardozo, speaking for this Court, said:

"The business of loading and unloading, being interstate or foreign commerce, the State of Washington is not at liberty to tax the privilege of doing it by exacting in return therefor a percentage of the gross receipts." (Citing numerous cases).

Again in *Gwinn, White & Prince v. Henneford,* 305 U. S. 434, 83 L. Ed. 272, reversing 193 Wash. 451, 75 P. 2d 1017, this Court made this same holding as to this same tax on the gross receipts of the business of marketing fruit. Justice Stone, speaking for this Court, said:

"But it is enough for present purposes that under the Commerce Clause, in the absence of congressional action, state taxation, whatever its form, is precluded if it discriminates against interstate commerce *or undertakes to lay a privilege tax measured by gross receipts derived from activities in such commerce* which extend beyond the territorial limits of the taxing state. Such a tax . . . burdens the commerce in the same manner and to the same extent as if the exaction were for the privilege of engaging in interstate commerce and would, if sustained, expose it to multiple tax burdens, each measured by the entire amount of the commerce, to which local commerce is not subject. . . The present tax, though nominally local, thus in its practical operation discriminates against interstate commerce, since it imposes upon it, merely because interstate commerce is being done, the risk of a multiple burden to which local commerce is not exposed." (Citing cases).

Now for the fourth time this Court should make the same holding as to the same tax directly applied to the gross receipts of the petitioners' interstate business.

In *McLeod v. Dilworth Co.*, 322 U. S. 327, 88 L. Ed. 1304, this Court held that imposition of the Arkansas sales tax upon sales of a Tennessee company to purchasers in Arkansas was unconstitutional in violation of the Commerce Clause, saying:

> "In this case the Tennessee seller was through selling in Tennessee. We would have to destroy both business and legal notions to deny that under these circumstances the sale—the transfer of ownership—was made in Tennessee. For Arkansas to impose a tax on such transaction would be to project its powers beyond its boundaries and to tax an interstate transaction. . . In view of the differences in the relation of the taxing state to them, a tax on an interstate sale like the one before us . . . involves an assumption of power by a State which the Commerce Clause was meant to end. The very purpose of the Commerce Clause was to create an area of free trade among the several States. That clause vested the power of taxing a transaction forming an unbroken process of interstate commerce in the Congress, not in the State."

In *Freeman v. Hewit*, 329 U. S. 249, 91 L. Ed. 265, this Court held that an Indiana tax on interstate sales of intangible securities infringed the Commerce Clause. Justice Frankfurter, speaking for this Court, said:

> "A State is also precluded from taking any action which may fairly be deemed to have the effect of impeding the free flow of trade between States. It is immaterial that local commerce is subjected to a similar encumbrance. . .
>
> "It cannot justify what amounts to a levy upon the very

process of commerce across State lines by pointing to a similar hobble on its local trade. . .

"And where, as in this case, the commodities subsequently sold interstate are securities, they can be reached by property tax *by the State of domicile of the owner. Virginia v. Imperial Coal Sales Co.*, 293 U. S. 15, 19, 79 L. Ed. 171, 174; 55 S. Ct. 12; and see *Citizens Nat. Bank v. Durr*, 257 U. S. 99, 66 L. Ed. 149, 42 S. Ct 15. . . .

"An exaction by a State from interstate commerce falls not because of a proven increase in the cost of the product. *What makes the tax invalid is the fact that there is interference by a state with the freedom of interstate commerce. . .*

"The tax on the sale itself cannot be differentiated from the direct unapportioned tax on gross receipts, which has been definitely held beyond the State taxing power ever since *Fargo v. Michigan. . .*

"There remains only the claim that an interstate sale of intangibles differs from an interstate sale of tangibles in respects material to the issue in this case. . . *Of course this is an interstate sale. And constitutionally it is commerce no less and no different because the subject was pieces of paper worth $65,214.20, rather than machines.*"

In the very recent case of *Central Greyhound Lines v. Mealey*, 334 U. S. 653, 92 L. Ed. (Adv. Op.) 1235, this Court held unconstitutional under the Commerce Clause a New York State tax on the gross receipts of a bus company passing through New Jersey and Pennsylvania while going between two points in New York, even though the

state court did not directly decide the constitutional question. Justice Frankfurter, speakinp for this Court. said:

> "The vice of such a tax is that it lays 'a direct burden upon every transaction in interstate commerce by withholding, for the use of the state, a part of every dollar received in such transaction.'" (Citing cases).

In *Joseph v. Carter & W. Stevedoring Co.*, 330 U. S. 422, 91 L. Ed. 993, this Court followed and reaffirmed *Puget Sound Stevedoring Co. v. State Tax Commission*, 302 U. S. 90, 82 L. Ed. 68, *supra*, and held such a tax on the gross receipts of a stevedoring company is unconstitutional. Justice Reed, speaking for this Court, said:

> "Although state laws do not discriminate against interstate commerce or in actuality or by possibility subject it to the cumulative burden of multiple levies, those laws may be unconstitutional because they burden or interfere with commerce. . . Stevedoring, we conclude, is essentially *a part of the commerce itself* and therefore a tax upon its gross receipts or upon the privilege of conducting the business of stevedoring for interstate and foreign commerce, measured by those gross receipts, is invalid. . . Such a rule may in practice prohibit a tax that adds no more to the cost of commerce than a permissible use or sales tax. . . The avoidance of such a local toll on the passage of commerce through a locality was one of the reasons for the adoption of the Commerce Clause."

See also to the same effect:

Adams Mfg. Co. v. Storen, 304 U. S. 307, 82 L. Ed. 1365; *Baldwin v. Seelig*, 294 U. S. 511, 79 L. Ed. 1032; *Nippert v.*

Richmond, 327 U. S. 416, 90 L. Ed. 760; *Toomer v. Witsell*, 334 U. S. 385, 92 L. Ed. (Adv. Op.) 1131; *Cheney Bros. Co. v. Massachusetts*, 246 U. S. 147, 153, 62 L. Ed. 632, 636; *Crew Levick Co. v. Pennsylvania*, 245 U. S. 292, 62 L. Ed. 295; *Best & Co. v. Maxwell*, 311 U. S. 454, 85 L. Ed. 275; *State ex rel Cruse v. American Can Co.*, 117 Colo. 312, 186 P. 2d 779.

The business of the petitioners in executing in California these written sales and license-royalty contracts and transmitting the same by mail to the purchasers in Washington, *constitutes interstate commerce.*

As stated by Chief Justice Marshall in *Gibbons v. Ogden*, 9 Wheat. 1, 189, 6 L. Ed. 23, 68:

> *"Commerce is undoubtedly traffic; but it is something more—it is intercourse."*

In *U. S. v. Southeastern Underwriters Assn.*, 322 U. S. 533, 88 L. Ed. 1440, this Court held that insurance contracts executed by residents of different states constitute interstate commerce and come with the Commerce Clause of the Constitution, saying:

> "One reason advanced for the rule in the Paul case has been that insurance policies 'are not commodities to be shipped or forwarded from one state to another.' But both before and since *Paul v. Virginia* this Court has held that *Congress can regulate traffic though it consists of intangibles.*"

In *Santa Cruz Fruit Packing Co. v. N. L. R. B.*, 303 U. S. 453, 82 L. Ed. 954, Chief Justice Hughes, speaking for this Court, said:

> "There is no question that petitioner was directly and largely engaged in interstate and foreign commerce. We have often decided that *sales to purchasers in another state* are not withdrawn from federal control because the goods are delivered f.o.b. at stated points within the state of origin for transportation." (Citing cases).

In *Dahnke-Walker Milling Co. v. Bondurant*, 257 U. S. 282, 66 L. Ed. 239, this Court said:

> "*Such commerce is not confined to transportation from one state to another, but comprehends all commercial intercourse between different states and all the component parts of that intercourse.*"

See also to the same effect:

Fisher's Blend Station v. Tax Commission, 297 U. S. 650, 80 L. Ed. 956, *supra; Freeman v. Hewit*, 329 U. S. 249, 91 L. Ed. 265, *supra; International Textbook Co. v. Pigg*, 217 U. S. 91, 54 L. Ed. 678; *Lemke v. Farmer's Grain Co.*, 258 U. S. 50, 66 L. Ed. 458; *U. S. v. Reading Co.*, 226 U. S. 324, 57 L. Ed. 243; *United Fuel Gas Co. v. Hallanan*, 257 U. S. 277, 66 L. Ed. 234; *Standard Oil Co. v. Johnson*, 33 Cal. App. 2d 430, 92 P. 2d 470; *15 C. J. S.* 257, sec. 1.

2. PATENT ROYALTIES ARE INCOME FROM INTANGIBLE PROPERTY AND TAXABLE ONLY IN STATE OF PATENTEE'S DOMICILE

It is undisputed that the domicile of the petitioners is in California. Patent royalties constitute income from patents which are intangible property. To tax the same, as in this case, outside of the state of the patentee's domicile is to extend the vicious evil of illegal double or multiple taxation and deprives the petitioners of their liberty and property without due process of law in violation of the Fourteenth Amendment of the Constitution. The situs of intangible property for tax purposes is the domicile of the owner under the well settled principle of *mobilia sequunter personam.*

This Court has repeatedly adhered to these principles as to intangible property such as stocks and bonds and and income therefrom.

Farmer's Loan & Trust Co. v. Minnesota, 280 U. S. 204, 74 L. Ed. 371; *Beidler v. South Carolina Tax Commission,* 282 U. S. 1, 75 L. Ed. 131; *Baldwin v. Missouri,* 281 U. S. 586, 74 L. Ed. 1056; *First National Bank v. Maine,* 284 U. S. 312, 76 L. Ed. 313.

This principle was recognized in *Suburban Transp. System v. King County,* 160 Wash. 364, 295 Pac. 124, quoting 26 R.C.L. 273, and in *Pacific Cold Storage Co. v. Pierce County,* 85 Wash. 626, 149 Pac. 34.

A case directly in point is *Newport Co. v. Wisconsin Tax Commission*, 219 Wis. 293, 261 N. W. 884, 100 A.L.R. 1204. It was approved by this Court by denial of certiorari in *Wisconsin Tax Commission v. Newport Co.*, 297 U. S. 720, 80 L. Ed. 1004. The Court held that the State of Wisconsin could not constitutionally under the Due Process Clause of the Constitution tax income derived from patent rights owned by the plaintiff, a Delaware corporation, even though it was licensed to do business in Wisconsin and the patented inventions were made through research at its Wisconsin manufacturing plant. That case was not as strong as this in favor of the taxpayer because here there is no question but that these inventions were made in California and not as a result of any research work or manufacturing activities in Washington. The Court quoted and followed the foregoing decisions of this Court, and said:

> "The difficulty is created by the fact that the discovery in this case culminated in the issuance of *letters patent*—in the creation of *intangible property* the income from which is by statute given a situs at the residence of the owner or recipient, and which is said by the United States supreme court to *have a situs at the domicile of the owner*. May this patent be treated, by reason of the place and circumstances of its discovery, as having a situs in Wisconsin? We think not. The taxpayer was not engaged in Wisconsin in the business of dealing in letters patent. *The intangible known as a patent had no more existence in Wisconsin* than any other intangible has existence at the loca-

tion of the tangible property to which it evidences rights."

See also *Freeman v. Hewit*, 329 U. S. 249, 91 L. Ed. 265, *supra*, and the cases there cited.

3. PATENT ROYALTIES ARE NOT PART OF THE SELLING PRICE.

In *Thys v. Rivard*, 25 Wn. 2d 345, 171 P. 2d 255, and 29 Wn. 2d 502, 187 P. 2d 652, an action to recover patent royalties under this same contract, the court recognized that these patent royalties were patent royalties and that the law of patents applied and governed the case. In this action, however, the court declined to recognize that principle.

There is a well established distinction between a royalty as compensation for a license for the use of a patented article and the selling price of a chattel, whether patented or unpatented. This distinction should be recognized in the field of taxation as elsewhere. These patent royalties were not part of the selling price, and the court seriously erred in holding that they were.

In each of these transactions title passed and the full selling price was paid when the machine was delivered to the purchaser. The purchaser acquired title, possession, and the right of possession. However, the machine em-

bodied the Thys patents, which gave petitioners *the exclusive right* to manufacture, sell, *and use* the same during the statutory seventeen-year period. It was for that reason that the license was issued. The royalty was merely compensation for the license or contractual right to use the patented machine.

The written agreement between petitioners and each of the machine purchasers (Pltf. Ex. 8) clearly shows that in fact the same contained two contracts in one instrument: (1) a contract for the sale of the machine and (2) a license contract for the use of patents embodied therein and an agreement to pay royalties to petitioners in consideration therefor.

A consideration of the contract, and particularly paragraphs 1, 3, 5 and 8 thereof, leaves no doubt but that title to the machine passed to the purchaser upon delivery. The full purchase price was always paid at or prior to delivery. The intention of the parties was clear that title passed to the purchaser at that time. A conditional sales contract was never signed or filed. There was no language or provision indicating any retention of title to the mahine by petitioners, either as security or otherwise.

Moreover obviously when a chattel is sold, it is necessary that the parties know the selling price thereof. If respondent were correct that the royalty were part of the

selling price, the parties could not know the amount of the selling price at the time of the sale or at the time of passing of title and delivery, for the reason that the royalty would vary, depending upon the quantity of hops picked thereby annually during a future seventeen year period. Under these circumstances we submit that it is absurd to contend that the royalties were part of the selling price.

Furthermore petitioners have paid and rightfully paid income tax based upon the royalty income. Certainly it would not be right that petitioners should have to pay income tax on the full amount of the royalties as such and yet that the same be considered part of the selling price, as gross proceeds of sale, of course, would not all constitute taxable income.

Also from the standpoint of the purchaser, if the royalty were part of the purchase price, it would be necessary to capitalize the same and the same could not be deducted as an operating expense. However, the royalty for the use of the hop picking machine is substantially the equivalent of payment to hand-labor for picking hops, and therefore should be considered an operating expense rather than a capital expenditure.

It is well settled that in construing tax statutes, all doubts are to be resolved against the government or state and the same are to be construed most strongly in favor

of the taxpayer. *Old Colony R. Co. v. Commissioner*, 284 U. S. 552, 76 L. Ed. 484; *Gould v. Gould*, 245 U. S. 151, 62 L. Ed. 211.

The Old Colony case also recognizes the well settled principle that the language of a tax statute should be given a fair and reasonable construction according to its plain and rational meaning. Applying these principles, the decision below was clearly erroneous.

The majority opinion does not cite any sustaining authority which has ever previously held that patent royalties are not patent royalties but are merely part of the selling price. So far as we are aware, no court has ever previously so held.

So zealously have the courts upheld the rights of inventors and patentees, pursuant to Art. I, sec. 8, clause 8, of the Constitution and the Federal Patent Statutes, title 35, U.S.C.A., sec. 31, et seq., that until 1932 *(Fox Film Corp. v. Doyal*, 286 U. S. 123, 76 L. Ed. 1010) it was settled law that no state could constitutionally under any circumstances tax patent royalties. See *Long v. Rockwood*, 277 U. S. 142, 72 L. Ed. 145, and cases there cited. Both the Fox and Long cases reognize that patent royalties are to be considered as such, and not as part of the selling price of a chattel.

In the *Five Per Cent Cases,* 110 U. S. 471, 478, 28 L. Ed. 198, this Court said:

> "A sale, in the ordinary sense of the word, is a transfer of property *for a fixed price* in money or its equivalent."

This has been many times quoted with approval, including *U. S. v. Benedict,* (CCA) 280 Fed. 76, 80; *Hale v. Helvering,* (CCA) 85 F. 2d 819; and *Estate of Edwin W. Rickenberg,* 11 T. C., decided July 7, 1948.

This royalty was payment for a license rather than a sale. *Arnold v. North American Chemical Co.,* 232 Mass. 196, 122 N. E. 283.

As stated by this Court in *Burnett v. Harmel,* 287 U. S. 103, 77 L. Ed. 199:

> "Moreover, the statute speaks of a 'sale' and these leases would not generally be described as a 'sale' of the mineral content of the soil, using the term either in its technical sense or as it is commonly understood. Nor would the payments made by lessee to lessor generally be denominated the purchase price of the oil and gas. By virtue of the lease, the lessee acquires the privilege of exploiting the land for the production of oil and gas for a prescribed period; he may explore, drill and produce oil and gas, if found. Such operations with respect to a mine have been said to resemble a manufacturing business carried on by the use of the soil, to which the passing of title of the minerals is but an incident, rather than a sale of the land or of any interest in it or in its mineral content. . .

> *"Such a construction . . . would have adopted a distorted, rather than the common meaning of the term 'sale,' . . .*
>
> "Bonus and royalties are both consideration for the lease and are income of the lessor. We cannot say that such payments by the lessee to the lessor, to be retained by him regardless of the production of any oil or gas, are any more to be taxed as capital gains than royalties which are measured by the actual production."

It is well settled that royalties are subject to the federal income tax as ordinary income and not as capital gains. *Burnet v. Harmel*, 287 U. S. 103, *supra*; *Estate of Ernest G. Hoffman*, 8 B. T. A. 1272, 1274; *Merten, Law of Federal Income Taxation*, vol. 3, p. 35, sec. 19.16, footnote 79, and vol. 8, p. 309, sec. 45.34; *Welder v. Commissioner*, (CCA) 148 F. 2d 583; *Zimbalist v. Anderson*, (CCA) 38 F. 2d 57; *Wood Process Co. v. Commissioner*, 2 T. C. 810, 816; *Sabatani v. Commissioner*, (CCA) 98 F. 2d 753; *General Motors Corp. v. Dailey*, (CCA) 93 F. 2d 938; *Commissioner v. Celanese Corp.*, (CCA) 140 F. 2d 339; *Cleveland Graphite Bronze Co. v. Commissioner*, 10 T. C. 974.

A contract to pay patent royalties may be lawfully combined with a contract for the sale of a patented machine, as was done here.

Porter Needle Co. v. National Needle Co., 17 Fed. 536; *Mitchell v. Hawley*, 16 Wall. 544; *Cold Metals Process Co.*

v. McLouth Steel Corp., 41 F. Supp. 487; *Schnack v. Applied Arts Corp.*, 283 Mich. 434, 278 N. W. 117; *Skee Ball Co. v. Cohen*, 286 Fed. 275; *Henry v. A. B. Dick Co.*, 224 U. S. 1, 56 L. Ed. 645, 654.

Transportation costs and similar charges paid by the purchaser are not part of the selling price. The same principle is applicable to these royalties.

Bloxom v. Henneford, 193 Wash. '540, 76 P. 2d 586; *Twaits v. State Tax Commission*, 106 Utah 343, 148 P. 2d 343; *Whitehill v. State Tax Commission*, 106 Utah 469, 150 P. 2d 370; *Dain Mfg. Co. v. State Tax Commission*, 237 Iowa 531, 22 N. W. 2d 786; and *Standard Oil Co. v. State Tax Commissioner*, 71 N. D. 146, 299 N. W. 447, 135 A. L. R. 1481.

4. PETITIONERS WERE NOT DOING BUSINESS IN WASHINGTON

It is undisputed that the petitioners did not reside or have any office, place of business, stock of merchandise, or authorized agent in Washington. Under the repeated decisions of this Court, they were not doing business there and were not subject to local taxation there.

People's Tobacco Co. v. American Tobacco Co., 246 U. S. 79, 62 L. Ed. 587; *Minnesota Commercial Men's Assn. v. Benn*, 261 U. S. 140, 67 L. Ed. 573; *Philadelphia & R. R. Co. v. McKibbin*, 243 U. S. 264, 61 L. Ed. 710; *Green v. C.*

B. & Q. R. Co., 205 U. S. 530, 51 L. Ed. 916; *Cheney v. Massachusetts*, 246 U. S. 147, 63 L. Ed. 632; *Bank of America v. Whitney*, 261 U. S. 171, 67 L. Ed. 594; *District of Columbia v. H. D. Lee Co.*, 161 F. 2d 646, cert. denied, 332 U. S. 760.

Petitioners had no control over the business of Lindeman Equipment Company, and the latter was an independent contractor and not an agent. *Chicago R. I. R. Co., v. Bond*, 240 U. S. 449, 60 L. Ed. 735; *Casement v. Brown*, 148 U. S. 615, 37 L. Ed. 532; *Doyle v. Union Pac. R. Co.*, 147 U. S. 413, 37 L. Ed. 223.

CONCLUSION

We therefore respectfully submit that not only is the decision below clearly erroneous, but also the same is of such nature that it should be reviewed and reversed in the proper exercise of the supervisory powers of this Court. The great national evils of interference with and obstruction to the free flow of interstate commerce transactions by the several states, double and multiple taxation of citizens, especially by states other than the domicile, interference by the states with the lawful constitutional rights of federal patent-holders—these evils will be promoted rather than retarded if this erroneous decision were to stand.

These are federal questions of substance and of great

public importance. The law should now be properly and authoritatively defined by this Court herein. The subject of state taxation of interstate commerce transactions should not be permitted to remain in its present confused condition. The highly salutary flow of free trade across state lines should not be subjected to multitudinous state tariffs. Washington should not be permitted to impose upon petitioners a tax for the privilege of engaging in interstate commerce between California and Washington—a right guaranteed to them under the Constitution. The issue is now directly presented to this Court, and its proper adjudication now will prevent similar future errors.

One of the tremendously important aims of our Federal Constitution and laws is to encourage invention and scientific and industrial progress by protecting the rights of patent-holders. Also the Commerce Clause and the Due Process Clause are the primary cornerstones of our constitutional structure. Preserving them inviolate and preserving the immunity of such interstate commerce from the burdens of state taxation, as contemplated by the Constitution, is, we believe, one of the high responsibilities of this honorable Court. The decision of the court below is an important step in the wrong direction. It is contrary to numerous decisions of this Court. It is unsound and opposed to the weight of authority. The same should not be permitted to stand.

Petitioners undoubtedly have a right to bring the case to this Court by an appeal as to the (first two) constitutional questions. We submit that this Court should grant certiorari in order that all four of these important legal questions may be authoritatively determined by this Court.

It is therefore respectfully submitted that this case is one calling for the exercise by this Court of its supervisory powers, by granting a writ of certiorari, and thereafter reviewing and reversing said decision.

Respectfully submitted,

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APPENDIX — STATE TAX STATUTE

The material portions of the state tax statute, namely, Titles II and III of the Revenue Act of 1935 (chap. 180) as amended by Laws of 1941, chap. 178 (Remington's Revised Statutes of Washington, 1941 Supplement, sections 8370-4 to 8370-25, and 8370-199, as amended) are as follows:

Rem. 1941 Supp. sec. 8370-4 reads in part as follows:

"From and after the first day of May, 1935, there is hereby levied and there shall be collected from every person a tax for the act or privilege of engaging in business activities. Such tax shall be measured by the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be, as follows: . . .

"(b) Upon every person engaging within this state in business as a manufacturer; as to such persons the amount of the tax with respect to such business shall be equal to the value of the products manufactured, multiplied by the rate of one-quarter of one per cent;

"The measure of the tax is the value of the products so manufactured regardless of the place of sale or the fact that deliveries may be made to points outside the state;

"(c) Upon every person engaging within this state in the business of making sales at retail; as to such persons, the amount of tax with respect to such business shall be equal to the gross proceeds of sales of the business, multiplied by the rate of one-quarter of one per cent; . . .

"(e) Upon every person except persons taxable under

subsection (d) above engaging within this state in the business of making sales at wholesale; as to such persons the amount of tax with respect to such business shall be equal to the gross proceeds of sales of such business multiplied by the rate of one-quarter of one per cent; . . .

Laws of 1941, chapter 178, §2, p. 482 (Rem. Supp. 1941, §8370-5 (P. P. C. §965-3), provides, *inter alia*:

"For the purposes of this title, unless otherwise required by the context: . . .

"(c) The word 'sale' means any transfer of the ownership of, title to, or possession of property for a valuable consideration and includes any activity classified as a 'sale at retail' or 'retail sale' under sub-section (d) of this section. It includes conditional sale contracts, leases with option to purchase, and any other contract under which possession of the property is given to the purchaser but title is retained by the vendor as security for the payment of the purchase price. It shall also be construed to include the furnishing of food, drink, or meals for compensation whether consumed upon the premises or not; . . .

"(f) The term 'gross proceeds of sales' means the value proceeding or accruing from the sale of tangible personal property without any deduction on account of the cost of property sold, the cost of materials used, labor costs, interest, discount paid, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses; . . .

"(h) The terms 'value proceeding or accruing' means the consideration, whether money, credits, rights or other property expressed in terms of money, actually received or accrued. The term shall be applied, in each

case, on a cash receipts or accrual basis according to which method of accounting is regularly employed in keeping the books of the taxpayer. The Tax Commission may provide by regulation that the value proceeding or accruing from sales on the installment plan under conditional contracts of sale may be reported as of the dates when the payments become due; . . .

"(j) The word 'manufacturer' means every person who, either directly or by contracting with others for the necessary labor or mechanical services, manufactures for sale or commercial use from his own materials or ingredients any articles, substances or commodities. When the owner of equipment or facilities furnishes, or sells to the customer prior to manufacture, all or a portion of the materials that become a part or whole of the manufactured article, the Tax Commission shall prescribe equitable rules for determining tax liability;

"(k) The term 'to manufacture' embraces all activities of a commercial nature wherein labor or skill is applied, by hand or machinery, to materials so that as a result thereof a new, different or useful article of tangible personal property or substance of trade or commerce is produced and shall include the production or fabrication of special made or custom made articles; . . ."

"(m) The word 'business' includes all activities engaged in with the object of gain, benefit or advantage to the taxpayer or to another person or class, directly or indirectly;

"(n) The term 'engaging in business' means commencing, conducting or continuing in business and also the exercise of corporate or franchise powers, as well as liquidating a business when the liquidators thereof hold themselves out to the public as conducting such business;"

"From and after the 1st day of May 1941, there is hereby levied and there shall be collected a tax on each *retail sale in this state* equal to three per cent of *the selling price.*" (sec. 8370-16).

"For the purposes of this title, unless otherwise required by the context:

"(a) The term 'selling price' means the consideration, whether money, credits, rights, or other property, expressed in the terms of money, paid or delivered by a buyer to a seller, and without any deduction on account of the cost of tangible property sold, the cost of the materials used, labor costs, interest, discount, delivery costs, taxes or any other expenses whatsoever paid or accrued and without any deduction on account of losses;" (sec. 8370-17).

"In the case of installment sales and leases with an option to purchase, the Commission, by regulation, may provide for the collection of taxes upon the installments of the purchase price, or amount of rental, as of the time the same fall due.

"In case the consideration for the lease with an option to purchase is not a bona fide consideration or does not represent a reasonable charge therefor, or if the agreement designated as a lease with an option to purchase is in fact not a true lease with an option to purchase, the Tax Commission shall issue equitable rules and regulations for the proper classification of such transaction.

"The Tax Commission, by general regulation, may provide that a taxpayer whose regular books of account are kept on a cash receipt basis may file returns based upon his cash receipts for each bi-monthly period and pay the tax herein provided upon such basis in lieu

of reporting and paying the tax on all sales made during such period." (Sec. 8370-25).

"Any person . . . having paid any tax as required by this act and feeling aggrieved by the amount of the tax may appeal to the superior court of Thurston County, within one year after the payment of such tax, or within thirty days after the date of the notice denying such a hearing or after the date of the order provided in this section. In the appeal the taxpayer shall set forth the amount of the tax imposed upon him, which he concedes to be the correct tax and the reason why the tax should be reduced or abated. The appeal shall be perfected by serving a copy of the notice of appeal upon the Tax Commission within the time provided and by filing the original thereof with proof of service with the clerk of the superior court of Thurston County. . . . The trial in the superior court on the appeal shall be *de novo* and without the necessity of any pleadings other than the notice of appeal. The burden shall rest upon the taxpayer to prove that the tax as paid by him is incorrect, either in whole or in part, and to establish the correct amount of the tax. In such proceeding the taxpayer shall be deemed the plaintiff, and the State of Washington, the defendant; and both parties shall be entitled to subpoena and require the attendance of witnesses as in other civil actions and to produce evidence that is competent, relevant and material to determine the correct amount of the tax that should be paid by the taxpayer under this act. Either party shall be allowed to appeal to the supreme court in the same manner as other civil actions are appealed to that court. It shall not be necessary for the taxpayer to protest against the payment of any tax or to make any demand to have the same refunded or to petition the Tax Commissioner for a hearing in order to appeal to the superior court, as herein provided; but no court action or proceeding of any kind shall be maintained

by the taxpayer to recover any tax paid, or any part thereof, except as herein provided." (Rem. Rev. Stat., Supp., sec. 8370-199, as amended by Laws of 1939, chap. 225, sec. 29).

Supreme Court of the United States

October term, 1948

No.....

ED THYS and ALBERT K. MILLER, co-partners doing business as THYS & MILLER,

Petitioners,

vs.

THE STATE OF WASHINGTON,

Respondent.

BRIEF IN OPPOSITION TO THE PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF WASHINGTON

SMITH TROY,
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THE STATE OF WASHINGTON,

Respondent.

BRIEF IN OPPOSITION TO THE PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF WASHINGTON

ADDITIONAL STATEMENT OF THE CASE

This case involves the application of the Washington State retail sales tax and the Washington State business and occupation tax to the proceeds of the sales of certain hop-picking machines *manufactured in the State of Washington and sold to purchasers in the State of Washington.* (R. 2, 34, 35, 58, 84, 85, 124, 127).

It has at no time been denied by petitioners that the Washington State sales tax and the business and occupation tax properly apply to the selling price of the machines, and petitioners voluntarily paid all such taxes with respect to

that portion of the consideration involved which they considered to be the "selling price." (R. 2, 9, 16, 21, 22, 23, 24, 39, 41, 42-43, 48, 51, 71, 94, 108, 110, 111, 112). The only issue in the case was and is as to whether certain amounts paid by the purchasers as "royalties" were not in fact part of the selling price of the machines and taxable as such. (R. 2, 16, 23, 24, 39, 51, 110, 111, 112).

The contracts of sale provided that the purchasers should pay, in addition to the basic amount denominated as the selling price (which amount was actually the mere cost of each machine to petitioners—R. 58, 91, 105, 108, 112), certain "royalties" for the right to use said machine. The royalties were based upon the quantity of hops harvested, but with a minimum "royalty," usually in the amount of five hundred dollars a year, being payable each year. (R. 109, 110). The state supreme court held that the *minimum* "royalty" payments, which are payable without regard to whether or not the machines are actually used, constitute part of the selling price of the machine and are taxable as such. To quote directly from the state supreme court's opinion, so that there may be no possible question on that point:

> "Under the circumstances here shown, the so-called 'royalties', *in so far as the payments of five hundred dollars a year are concerned*, are, in effect, a part of the cost of the machine and of the right to use the same to the purchaser. *The minimum payment of five hundred dollars a year* (or some other sum) *required in any event* is, in effect, a payment simply for the right to use the machine and is not based upon any actual use thereof, ..." (Emphasis Added) (R. 120).
>
> "WE HOLD that, under the contracts whereby respondents sold the hop-picking machines within this state, the so-called 'royalties' (*referring to the payments of five hundred dollars a year, regardless of the use or*

non-use of the machine) are, for the purposes of the statutes of this state providing for the payment of a sales tax, part of the selling price of the machine and taxable as such . . . ." (Emphasis added) (R. 125)

As we have already pointed out, the machines in question were manufactured in the state of Washington for petitioners and on their order. (R. 2, 34, 35, 84, 124, 127). The manufacturing operation was financed entirely by petitioners, who maintained a bank account in this state from which the manufacture of the machines was financed. (R. 37, 49, 50, 87, 106, 107, 127). During the course of manufacture and until sold, the machines and their component parts were at all times the property of petitioners (R. 29, 34-35, 105, 127), and were required to be and were insured for their protection (R. 85, 105). One of petitioners regularly came to the state of Washington several times a year to test and inspect the machines during the course of construction. (R. 28, 88, 108). The "royalties" were collected and checked in the state of Washington by a representative (R. 61, 100, 110, 127) who is a resident of the State of Washington (R. 99).

In selling the machines, the so-called selling price (as to which tax liability is conceded) was the amount paid by the petitioners for the construction of the machines. (R. 58, 91, 105, 108, 112). In other words, the so-called selling price fixed in the contracts of sale by petitioners to their vendees actually represented the cost of the machines to petitioners (in which cost, however, was included a charge of $500 made by petitioners for engineering and supervising services (R. 106)). Aside from the charge made for engineering and supervising services, petitioners' profit on the sale of the machines came entirely in the so-called "royalties,"

with the "royalty" provision of the contracts calling for a *minimum* payment of $500 a year. And, as we have pointed out, it is those minimum royalties only that the state supreme court held to be taxable as part of the selling price of the machines, since they are payable without regard to actual use.

ARGUMENT

I. The Proceedings in the State Courts Are Not Yet Final

The court's attention is respectfully directed at the outset to the following especially significant portion of the judgment which petitioners seek to have reviewed:

> ". . . the cause [is] remanded to the superior court, *with instructions to proceed as directed by the opinion* . . ." (Emphasis added) (R. 139).

The instructions to which the express reference is made in the judgment (and which instructions are thus incorporated into the face of the judgment by necessary reference—*Clark v. Williard*, 292 U. S. 112, 78 L. Ed. 1160, 54 S. Ct. 615 (1934)), are contained in the last paragraph of the court's opinion, which paragraph reads as follows:

> "The judgment appealed from is reversed, and the cause remanded to the superior court, *with instructions to reopen the case* and, upon the record already made before the superior court *and such other evidence as may be introduced by either party or both parties*, in accordance with the views herein expressed, determine the amount of taxes due the state, for which respondents are liable, based upon the record herein, as amplified by other evidence, if any be introduced." (Emphasis added) (R. 130).

We submit that it is apparent from the face of the judgment itself that it does not have the finality that constitutes a jurisdictional prerequisite to any review of the judgment by this honorable court.

Grays Harbor Logging Co. v. Coats-Fordney Logging Co., 243 U. S. 251, 61 L. Ed. 702, 37 S. Ct. 295 (1917).

Bruce v. Tobin, 245 U. S. 18, 62 L. Ed. 123, 38 S. Ct. 7 (1917).

"It is also stated as a general rule that the judgment must be complete as well as final, and must finally dispose of all elements of the controversy . . .

" . . . And even if the judgment of the state supreme court is final in the sense that it determines the ultimate right of the plaintiff and the general principles by which it is to be measured, it is not final if it reverses the judgment of the trial court rejecting the claim and remands for new trial, although the only issue open on retrial is the amount of recovery." Robertson and Kirkham, *Jurisdiction of the United States Supreme Court*, Sec. 30.

" . . . Similarly, a state court judgment is not final when it determines all the principles governing the rights and liabilities of the parties, but refers the case to a master or court for an accounting. And even though a judgment of reversal limits the new trial to the question of the amount of damages, the judgment is not final, and is no more reviewable than one which awards a new trial on the whole case.

"Whatever means may be employed for remitting some particular issue for further proceedings, the unfinished state of the case will prevent the judgment from being final. . . ." Boskey, *"Finality of State Court Judgments Under the Federal Judicial Code,"* 43 Columbia Law Review 1002, 1009.

"A judgment or decree of the highest court of a state, reversing an inferior court and remanding the case to the lower court for a new trial or for further proceedings consistent with the judgment of the appellate court, is not a final judgment, and cannot be reviewed by the Federal Supreme Court. . . . [Citing 26 decisions to that effect] . . ." Subdivision III, entitled *"Judgment reversing, or remanding for new trial or further proceedings, generally"*, of annotation entitled *"When judgment of state court in civil cases is final for purpose for review by Supreme Court of United States"*. 89 L. Ed. 1186, 1188.

See, also:

54 Am. Jur. 820, United States Courts, Sec. 186; 36 C. J. S. 147, Federal Courts, Sec. 240; Cyclopedia of Federal

Procedure (2d ed.) Vol. 10, Sec. 4976, p. 366; Hughes Federal Practice, Vol. 5, Secs. 3191, 3192, p. 290 *et seq.*; and Simkins Federal Practice (3rd ed.), Sec. 962, p. 682; Note, *"Finality of Decree for Purposes of Review in the Supreme Court"*, 48 Harv. L. Rev. 302.

2. No Substantial Federal Question Is Involved

It is submitted that no substantial federal question is involved in the case at bar.

As has been pointed out, the machines in question were at all times within the state of Washington, and petitioners have at no time denied—they couldn't deny—that the sales tax and the business and occupation tax were properly payable upon what petitioners denominated as the "selling price" of the machines. The only dispute was as to the proper method of *computation* of the admitted state tax liabilities in issue. And questions relative to the proper method of *computation* of state taxes (as distinguished from questions relative to *applicability* of the taxes) are, we submit, essentially local questions, not federal ones.

Had petitioners sold their machines for a single, flat amount, there would not be and there could not be the slightest possible question but that the taxes in issue must be computed by the entire sales price. The arbitrary segregation by petitioners of the consideration payable by the purchasers of the machines into a basic price plus "royalties" results in no change in the substance of the transactions and should not have any effect on the tax liability involved. The abuses that could stem from any other result are obvious. As the state supreme court pointed out in this very case:

". . . While the amount paid by the purchaser at the time of the execution of the contract doubtless

> fairly represented the cost of the machine, and a reasonable maker's profit for the material and work required to build a machine, if taxes upon the amounts to be paid subsequently by the purchaser might be avoided by the method used, a vendor might, by a contract similar in substance, sell a machine, without the right to use it, for much less than its cost, and, by providing for the payment of 'royalties,' receive the greater portion of the cost of the machine by way of such payments." (R. 120, 121).

Especially in so far as the *minimum* "royalty" payments are concerned, the transactions in issue amounted to nothing more than sales on an installment basis, and those installment payments constitute part of the taxable selling price both as a matter of logic and of express statutory provision.

The Washington State sales tax statute defines the term "selling price" as meaning

> ". . . the consideration, whether money, credits, rights, or other property, expressed in terms of money, paid or delivered by a buyer to a seller, . . ." (Sec. 17(a), Chapter 180, Laws of 1935, as last amended by Section 4, Chapter 249, Laws of 1945; Remington's Revised Statutes, 1945 Supplement, sec. 8370-17(a)).

The "royalties" in question are part of the consideration paid by the buyers of the machines, and they therefore constitute part of the "selling price" under the explicit terms of the statute. The pertinent provisions of the business and occupation tax statutes are similar in effect. (See the definitions of the terms "gross proceeds of sales" and "value proceeding or accruing", which are quoted on p. 42 of petitioners' petition).

Furthermore, in so far as the sales tax is involved (and it represents the greatest proportion of the amounts in issue—the sales tax rate being 3%, whereas the occupation tax rate is ¼ of 1%), the tax is actually imposed upon the

buyer. Petitioners are simply required to collect the tax for the state, and any question as to the *amount* that they are required to collect under the laws of this state on sales to purchasers in this state can by no stretch of the imagination be said to involve any federal question. The fact that the state supreme court interpreted the admittedly applicable state statutes as requiring the collection of a larger amount of tax than petitioners originally thought collectible results in no more of a federal question or problem than would an increase in the amount to be collected which might result from direct legislative action. And in so far as the occupation tax is concerned, the court's attention is invited to the fact that petitioners' contracts with their vendees provided that the vendees would pay "all sales taxes *and other excise taxes payable on the sale.*" (R. 108, 120). [The citations are to portions of the state supreme court's opinions. The exhibits in the case were evidently not printed as part of the record, although they were included in the "Designation of Record for Certiorari". (R. 139). The forms of sales contract used by petitioners are Exhibit 8. (R. 17, 18.)] In view of the contractual provision just quoted, it would appear that our last comments relative to the sales tax situation are equally applicable to the business and occupation tax phase of this matter.

3. Answer to Petitioners' Arguments

a. Petitioners' argument re interstate commerce.

In the first subdivision of petitioners' argument, they argue that "these taxes are an illegal and unconstitutional imposition upon interstate commerce." In their attempt to establish that proposition, they ignore the facts that the machines in question were manufactured in this state and were sold to purchasers and users in this state and that they

(petitioners) have at all times admitted their basic liability for the taxes at issue, and they place practically their entire reliance upon the fact that the contracts of sale were accepted by petitioners in California.

A series of relatively recent decisions by this court, however, definitely establishes that the state in which delivery of the goods is effected has full jurisdiction to tax the transaction, despite the fact that the contract may have been accepted in some other state. Specifically, this court has upheld sales taxes, use taxes, and gross income taxes when imposed by the state in which delivery of the goods was effected, despite the fact that the orders were accepted in another state (and despite the further fact, we might add, that the goods themselves moved in interstate commerce). The pertinent decisions are:

Sales taxes:

McGoldrick v. Felt & Tarrant Mfg. Co., 309 U. S. 70, 84 L. Ed. 584, 60 S. Ct. 404 (1940); *Jagels, "A Fuel Corporation" v. Taylor*, 309 U. S. 619, 84 L. Ed. 983, 60 S. Ct. 469 (1940), affirming, *per curiam*, 280 N. Y. 766, 21 N. E. (2d) 526 (1940);

Use taxes:

Felt & Tarrant Mfg. Co. v. Gallagher, 306 U. S. 62, 83 L. Ed. 489, 59 S. Ct. 376 (1939); *Nelson v. Sears, Roebuck & Co.*, 312 U. S. 359, 85 L. Ed. 888, 61 S. Ct. 586 (1941); and *General Trading Co. v. State Tax Commission*, 322 U. S. 335, 88 L. Ed. 1309, 64 S. Ct. 1028 (1944); and

Gross income taxes:

Department of Treasury v. Allied Mills, 318 U. S. 740, 87 L. Ed. 1120, 63 S. Ct. 666 (1943), affirming, *per curiam*, 220 Ind. 340, 42 N. E. (2d) 34.

It is interesting to note also that in two of the cases just cited (*Jagels, "A Fuel Corporation" v. Taylor, supra*; and *Nelson v. Sears, Roebuck, supra*) the orders had not even been solicited in the taxing jurisdiction, which is an additional factor upon which petitioners appear to be placing some reliance here.

For additional decisions in which the taxing jurisdiction of the state of the buyer was upheld despite the fact that *the goods themselves* moved in interstate commerce, see:

Graybar Electric Co. v. Curry, 308 U. S. 513, 84 L. Ed. 437, 60 S. Ct. 139 (1939), affirming *per curiam*, 238 Ala. 116, 189 So. 186 (sales tax); *International Harvester Co. v. Dept. of Treasury*, 322 U. S. 340, 88 L. Ed. 1313, 64 S. Ct. 1019 (1944) (gross income tax); and *McGoldrick v. Berwind-White Coal Mining Co.*, 309 U. S. 33, 84 L. Ed. 565, 60 S. Ct. 388 (1940) (sales tax).

b. Petitioners' argument re patent royalties.

The second and third subdivisions of petitioners' argument are both predicated, in effect, upon the contention that, in the language of the title of petitioners' third subdivision, the "patent royalties are not part of the selling price."

As we have already pointed out, the facts of the case refute that basic contention. The so-called "royalties" which the state supreme court held to be taxable as part of the selling price are the *minimum* yearly "royalties," which are payable to petitioners without regard to whether or not the machines are actually used. They are thus amounts that are payable by the buyers to petitioners as a result of the initial sale of the machines, and they consti-

tute part of the selling price as a matter of fundamental logic, to say nothing of the pertinent statutory provisions.

The only basis for petitioners' claim that these minimum "royalty" payments are not part of the selling price, is the self-serving fact that petitioners chose to label them as "royalties" in their contracts. In fact, however, the minimum annual payments are no different from an ordinary selling price which is payable in installments, and the different label that petitioners apply to those minimum annual payments cannot serve to convert a taxable portion of the selling price into non-taxable "royalties."

In addition, this phase of petitioners' argument is necessarily based upon the theory that *they* are being taxed improperly on *their* income from the so-called "royalties." But as we have already pointed out, the ultimate *sales* tax liability is upon the *purchasers*, and petitioners are merely required to collect the tax. The increased amount of tax that petitioners are required to collect under the decision by the state supreme court involves no more interference with their patent rights than did the collection of the lesser amount of tax as to which they at all times conceded their liability. And, again, by virtue of the provision in their contracts that the vendees would pay "all sales taxes *and other excise taxes* payable on the sale," (R. 108, 120), the same argument applies to the occupation tax involved.

The fundamental error in petitioners' argument is apparent from their citation of the case of *Newport Co. v. Wisconsin Tax Commission*, 219 Wis. 293, 261 N. W. 884, 100 A. L. R. 1204 (1935), as being "a case directly in point." The portion of that decision upon which petitioners rely involved the sale of patent rights as such—that is, the taxpayer sold those *intangibles* alone—and the court held that the intangibles had their situs at the domicile of the owner and that

the income from those sales therefore was not taxable in Wisconsin. In this case, on the other hand, we are concerned with *tangibles* which were manufactured and sold in the state of Washington, and the proceeds from the sales of which are *admittedly* subject to the taxes in issue, with the only question being whether or not the arbitrary designation of the minimum annual amounts payable by the buyers as "royalties" can serve to render them non-taxable, whereas if they were called installment payments of the purchase price there wouldn't be any question whatsoever as to the applicability of the taxes in issue. On the only real question in this case, i.e., as to the proper method of computation of taxes on the sale of *tangible* property manufactured and sold in this state, where part of the minimum consideration payable is arbitrarily designated in the contract as being a "royalty," the *Newport Co.* case, which petitioners refer to as "directly in point," has no bearing whatsoever.

c. Petitioners' argument re "doing business."

Petitioners contend that they were not doing business in the state of Washington, and therefore are not subject to local taxation here.

It will be noticed at the outset that this contention is entirely inconsistent with petitioners' basic position throughout this litigation, which was that it is only as to the so-called "royalties" that the taxes in issue do not apply. In so far as the sales involved the amounts which petitioners denominated as the selling price, the taxes were at all times collected and paid, and petitioners emphasized that fact repeatedly at all stages of the proceedings below. (R. 2, 9, 16, 21, 22, 23, 24, 39, 41, 42-43, 48, 71). To quote directly from the opening statement of counsel for petitioners at the trial of this action:

". . . The point in dispute here relates primarily, if not entirely, to whether or not the royalties for the use of the patented hop picking machines are taxable in this state. *So far as the three percent sales tax on what we call the original purchase price of the machine is concerned and the one-fourth of one percent occupation tax, there is no dispute as to that,* nor is there any dispute as to the relatively minor items of repair parts which are manufactured in California and shipped to this state, and which are subject to the three percent compensating tax, and those taxes have been fully paid. The dispute is as to whether or not the royalties are taxable. . . ." (R. 2).

The claim that petitioners were not doing business in this state is obviously inconsistent with petitioners' admission of liability with respect to "what [they] call the original purchase price," and this phase of their argument actually has no relevance to the only real issue in the case. Actually, the basic liability has at all times been admitted, and the only question has been as to the *extent* of the liability.

But aside from the inconsistency in petitioners' position, the record clearly establishes the fact that petitioners were, in fact, doing business in the state of Washington. The machines were regularly manufactured for them in this state. (R. 2, 34, 35, 84, 124, 127). The manufacturing operations were financed entirely by petitioners from a bank account which was maintained by them in this state. (R. 37, 49, 50, 87, 106, 107, 127). The machines and their component parts were at all times the property of petitioners, until sold (R. 29, 34-35, 105, 127), and were required to be, and were, insured for petitioners' protection (R. 85, 105). One of the petitioners regularly came to this state several times a year to test and inspect the machines during the course of construction. (R. 28, 88, 108). The royalties payable by users of the machines in this state were collected

and checked by a representative who is a resident of this state. (R. 61, 100, 110, 127).

Thus, petitioners regularly had machines, parts, a bank account, and a resident representative in this state. All of the activities were and are carried on as a regular course of business, and the substantial nature of those activities is indicated by the fact that the taxes voluntarily reported and paid by petitioners for the tax period in issue totalled $16,484.18 (R. 9).

In the light of the foregoing facts, which are not so much as mentioned by petitioners in this phase of their argument, the claim that they were not doing business in the state of Washington is clearly untenable.

CONCLUSION

Accordingly, it is respectfully submitted that the petition for certiorari be denied for the reasons that the proceedings in the state courts are not yet final and that no substantial federal question is involved.

Respectfully submitted,

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October Term, 1948

No. 720

THYS and ALBERT K. MILLER, co-partners doing business as THYS & MILLER,

Petitioners,

vs.

STATE OF WASHINGTON,

Respondent.

PETITION FOR REHEARING

ON PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF WASHINGTON

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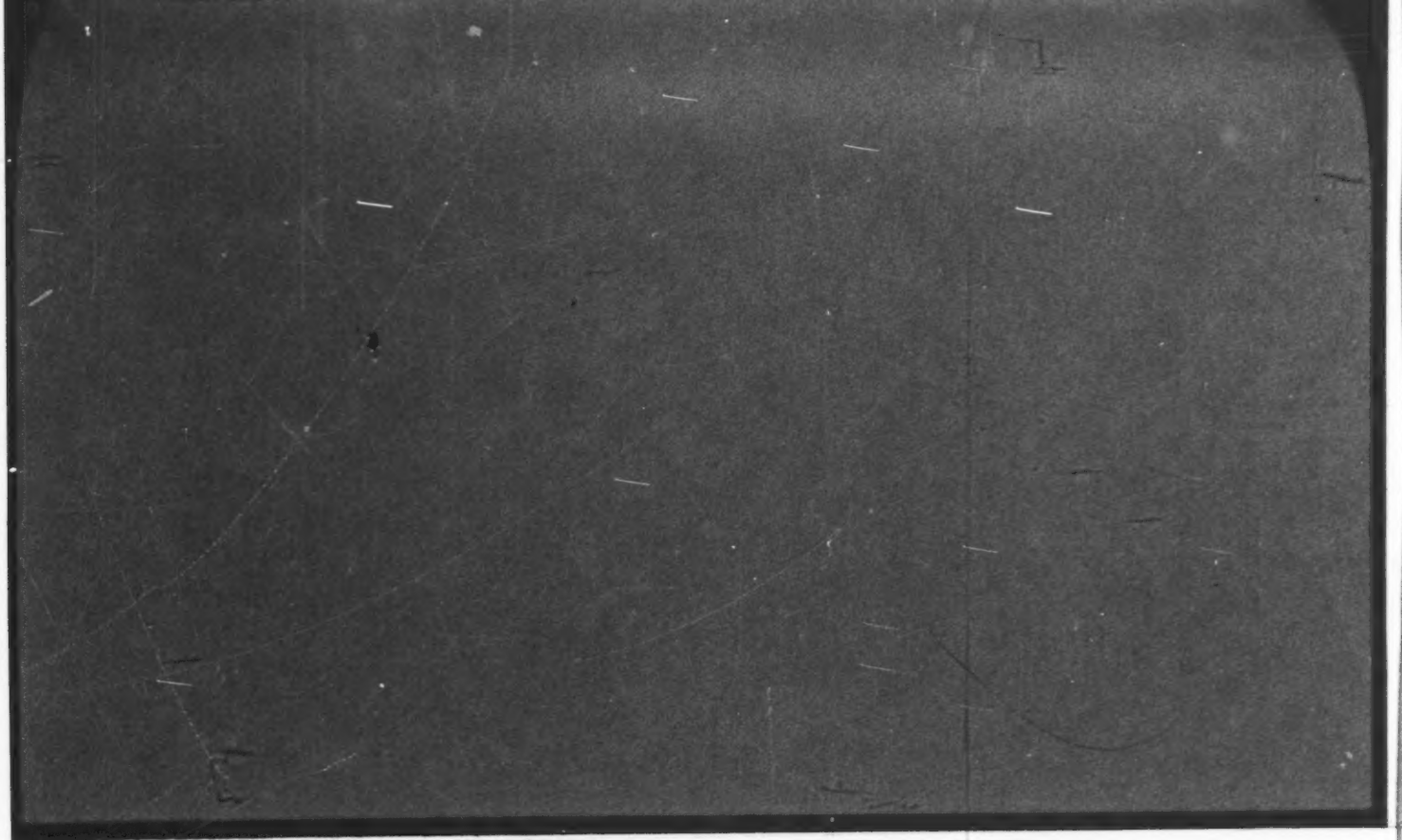

Supreme Court of the United States

October Term, 1948

No. 720

ED THYS and ALBERT K. MILLER, co-partners doing business as THYS & MILLER,

Petitioners,

vs.

STATE OF WASHINGTON,

Respondent.

PETITION FOR REHEARING

ON PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF WASHINGTON

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STATE OF WASHINGTON,

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PETITION FOR REHEARING OF PETITIONERS

Petitioners respectfully petition this Honorable Court for a rehearing herein, and urge that the cause be reconsidered and that the petition for writ of certiorari be granted and the judgment reversed.

This petition for rehearing is based upon other substantial grounds available to petitioners although not previously presented. *Schriber-Schroth Co. v. Cleveland Trust Co.*, 305 U. S. 47, 50. 83 L. Ed. 34, 36.

We assume that the decision of this Court denying the petition for writ of certiorari was based upon one or more of the alleged grounds for such denial urged in respondent's brief. Petitioners had prepared the reply brief thereto,

but unfortunately the decision was filed prior to the filing of said reply brief. This case is extremely important both to the parties and to the public by reason of the extremely important nature of the questions involved. The grounds and points urged in respondent's brief were not previously presented or discussed in our petition or our opening brief. We therefore deem it extremely important that the following matters be brought to the attention of this Court before there is a final determination herein.

1. THE JUDGMENT IS FINAL AND APPEALABLE.

Respondent's first contention (p. 9) that there is not a final appealable judgment, was not presented or discussed in our petition or opening brief.

We submit, however, that this is a final appealable judgment. Manifestly all of the legal and factual questions herein have heretofore been fully and finally determined in the state courts. The only possible purpose of a remand to the trial court—which has not been requested or desired by either party—would be for a mere mathematical computation (or at the most accounting) to determine exact amount of taxes due, if any. There is no additional evidence to introduce. There is no intention of or remand for a new trial.

Respondent quotes a law review article by one Boskey

(43 Col. L. Rev. 1002, 1009) that a state supreme court judgment is not final when it remands the case for an accounting. However, as hereinafter pointed out, *this Court has subsequently held to the contrary.*

We have examined the authorities cited by respondent and find that none of them is in point.

Grays Harbor Logging Co. v. Coates-Fordney Logging Co., 243 U. S. 251, 61 L. Ed. 702, merely held that an interlocutory order of use and necessity in a condemnation proceeding was not a final appealable judgment until judgment had been entered after a trial as to the amount of damages. The award of damages was held to be necessarily a condition of the right to take the property. As there pointed out, such an interlocutory order under the state law was not even a final judgment appealable to the state supreme court. In effect this is one of the "new trial" cases, as a further entire jury trial was necessary to determine the amount of damages. There had been no trial or hearing whatever pertaining to damages. The state constitution and statutes prohibited the transfer of the condemned property until after the compensation had been determined and paid. Thus the issue of the right to take was necessarily dependent for final resolution on the determination of the amount of compensation. The controversy was not severable into distinct phases. The case is obviously clearly distinguishable.

Boskey, "Finality of State Court Judgments under the Federal Judicial Code," 43 Col. Law Rev. 1002, 1007, states the reason for the Grays Harbor decision:

> "In the subsequent hearing on assessment of damages, new federal questions could arise, which would force the Supreme Court to review the case piecemeal if it were to assume jurisdiction upon a mere order for condemnation."

Of course, there is not the slightest possibility of that occurring in this case.

The portion of the Boskey article quoted by respondent has been overruled by this Court in the Johnson case hereinafter quoted. Moreover, the instant case comes directly within Boskey's qualification (by footnote) to the statement quoted by respondent:

> "*A different question would be presented if the judgment settled the rules governing the measure of damages and the record contained all the data necessary for ascertaining the ultimate amount, so that nothing remained to be done but the ministerial duty of making the indicated arithmetical computation. Such a judgment might well be final* under the rule of *Mower v. Fletcher,* 114 U. S. 127 (1885) . . . *Cf. Gulf Refining Co. v. United States,* 269 U. S. 125, 136." (All italics are ours).

Likewise, in *Bruce v. Tobin,* 245 U. S. 18, 62 L. Ed. 123, the state supreme court decision reversed a judgment of dismissal and remanded the case for *a new trial.* There had been no determination whatever as to the amount of

recovery. This case likewise is one of the new trial cases and is not at all in point here.

This case comes directly within the recent decision of this Court in *Radio Station WOW, Inc. v. Johnson*, 326 U. S. 120, 89 L. Ed. 2092, where this court overruled a challenge to its jurisdiction even though the state supreme court, which was reversed on certiorari, not only directed delivery of certain property, *but also ordered the case remanded to the trial court for an accounting.* The decision of this court upon this question was unanimous. Mr. Justice Frankfurter, speaking for this Court, said:

> "The problem of determining when a litigation is concluded so as to be 'final' to permit review here arises in this case because, as has been indicated, the Nebraska Supreme Court not only directed a transfer of property, *but also ordered an accounting of profits from such property.* . .
>
> "In short, the rationale of those cases is that a judgment directing immediate delivery of physical property is reviewable and *is to be deemed disassociated from a provision for an accounting even though that is decreed in the same order.* In effect, such a controversy is a multiple litigation allowing review of the adjudication which is concluded because it is independent of, and unaffected by, another litigation with which it happens to be entangled. . . .
>
> "That presumption in allowing such review is that *the Federal questions that could come here have been adjudicated by the State court, and that the accounting which remains to be taken could not remotely give rise*

to a Federal question. Of course, where the remaining litigation may raise other Federal questions that may later come here, such as is true of eminent domain cases, see *Grays Harbor Logging Co. v. Coats-Fordney Logging Co.* (Washington ex rel. Grays Harbor Logging Co. v. Superior Ct.) 243 U. S. 251, 61 L. Ed. 702, 37 S. Ct. 295, to allow review of an intermediate adjudication would offend the decisive objection to fragmentary reviews."

We sincerely believe and respectfully submit that the foregoing decision of this Court is conclusive. There is not the slightest question but that all of the federal questions that could come here have been heretofore adjudicated by the state supreme court. The mathematical computation, if any, (or the accounting, if any) which remain "*could not remotely give rise to a Federal question.*" The Johnson case is directly in point and decisive of this question here.

Also directly in point and conclusive is the recent unanimous (on this question) decision of this Court in *Richfield Oil Corp. v. State Board of Equalization,* 329 U. S. 69, 91 L. Ed. 80. The California supreme court had ordered the judgment reversed. Under the California law, where the judgment is reversed without directions, as in that case, there is a new trial. This Court, however, overruled the jurisdictional objection, reversed the state supreme court judgment, and held that the taxpayer was entitled to recover a refund of the state retail sales tax illegally assessed. Mr. Justice Douglas, speaking for this Court, said:

"The question is whether it can be said that 'there is nothing more to be decided' (Clark v. Williard, 292 U. S. 112, 118, 78 L. Ed. 1160, 1164, 54 S. Ct. 615), that there has been 'an effective determination of the litigation.' (Citing cases). That question will be resolved not only by an examination of the entire record (Clark v. Williard (U. S.) supra) but, where necessary, by resort to the local law to determine what effect the judgment has under the state rules of practice. (Citing cases). . . .

"The claim thus frames and restricts the issues for the litigation. Although the Supreme Court reversed the judgment of the trial court without direction, its decision controls the disposition of the case. (Citing cases). Since the facts have been stipulated and *the Supreme Court of California has passed on the issues which control the litigation, we take it that there is nothing more to be decided.* The jurisdictional objection is thus without merit."

In *Carondelet Canal & Nav. Co. v. Louisiana*, 233 U. S. 362, 58 L. Ed. 1001, in accepting jurisdiction and reversing a state supreme court decision which remanded the case for an accounting and for certain further proceedings, this Court said:

"The claims of the state to a triangular strip of ground hereafter mentioned, or to the proceeds thereof, or to any other property, movable or immovable, not appurtenant to the waterway and roadways, were reserved for further adjudication in the proceedings. And *an accounting was ordered* of the receipts and disbursements in the management of the property since March 10, 1908, and *the case was remanded to the district court for further proceedings* on all questions reserved as above stated, and 'that the right of

the plaintiff to obtain judgment for such amount as may be found due upon defendant's accounting, and to take such further orders as may be required for the execution of this judgment, be reserved.'

". . . . That is, all was decreed that it was the purpose of the suit to have decreed, and which not only constituted its success, but *which involved and disposed of the Federal right asserted by the canal company. The judgment, therefore, has a substantial finality.* Is it not as well in form? . . .

"In the case at bar *there is distinct and explicit finality,* and the further proceedings are directed to apply only to the 'questions reserved.' . . . The decree, therefore, had a definiteness which did not exist in the cited cases, the Federal rights asserted by the canal company were injuriously disposed of. The ground of dismissal of the writ of error based on the judgment is not, therefore, sustained."

This case also comes directly within the rule as recently stated by Mr. Justice Jackson rendering the unanimous decision of this Court in *Market Street Ry. Co. v. Railroad Commission,* 324 U. S. 548, 89 L. Ed. 1171:

"Final it must be in two senses: It must be subject to no further review or correction in any other state tribunal; it must also be final as an effective determination of the litigation and not of merely interlocutory or intermediate steps therein. It must be the final word of a final court.

". . . . *The judgment for our purposes is final when the issues are adjudged . . . . Our test is a practical one. When the case is decided, the time to seek our review begins to run.*"

The state statute governing the procedure in an action of this nature (Rem. Rev. Stat. Supp. sec. 8370-199, as amended by Laws of 1939, ch. 225, sec. 29) is quoted at page 45 in the appendix to our opening brief. Under this statute there is no occasion whatever for any new trial nor any further proceedings, aside from the mere mathematical computation and ministerial act of entering judgment pursuant to the supreme court decision, unless reversed.

In *Mower v. Fletcher*, 114 U. S. 127, 29 L. Ed. 117, quoted in annotation, 89 L. Ed. 1189, this Court held that it had jurisdiction where the state supreme court reversed the judgment with directions to enter a certain judgment in favor of the plaintiff. This court said:

> "The litigation is ended, and the rights of the parties on the merits have been fully determined. Nothing remains to be done but to require the inferior court to perform the ministerial act of entering the judgments in that court which have been ordered. This is but carrying the judgment of the Supreme Court, which has been rendered, into execution. Nothing is left to the judicial discretion of the court below."

In *Gulf Refining Co. v. U. S.*, 269 U. S. 125, 136, 70 L. Ed. 195, this Court said:

> "The instruction for further proceedings not inconsistent with the opinion, therefore, was equivalent to a direction to render judgment for the net value—that is, for the exact sums set forth in the stipulation. (Citing cases) . . . Nothing remains but the ministerial duty of entering a decree for the precise sums which had

been fixed beyond the power of alteration. It follows that the jurisdictional objection is without merit."

10 Cyclopedia of Federal Procedure (2d ed.) 369, sec. 4976, (cited by respondent) states:

"*However, the mere remand for further proceedings as to certain specific questions of a minor and collateral nature does not deprive the judgment of the requisite finality where, as to the major questions involved, including the federal questions, the judgment has a distinct and explicit finality in substance and form.*"

"*Where a judgment of the highest court of a state is final under decisions of that court, the Supreme Court of the United States treats it as final. Brady v. Terminal Railroad Assn.*, 302 U. S. 678, 82 L. Ed. 523." Ibid, p. 367, (footnote 62).

See also to the same effect:

LaCrosse Telephone Corp. v. Wisconsin Employment Relations Board, U. S., 93 L. Ed. (Adv. Op.) 265, 268 (decided January 17, 1949); *Parker v. Illinois*, 333 U. S. 571, 92 L. Ed. 886; *Dept. of Banking v. Pink*, 317 U. S. 268, 87 L. Ed. 257; *Cole v. Violette*, 319 U. S. 581, 87 L. Ed. 1599; *Rio Grande Western R. Co. v. Stringham*, 239 U. S. 44, 60 L. Ed. 136; *Clark v. Williard*, 292 U. S. 112, 78 L. Ed. 1160; *Tippecanoe County v. Lucas*, 93 U. S. 108, 23 L. Ed. 822; *Knox Natl. Farm Loan Assn. v. Philips*, 300 U. S. 194, 81 L. Ed. 599; *Brady v. Terminal Railroad Assn.*, 302 U. S. 678, 303 U. S. 10; *Driver's Union v. Meadowmoore*, 312 U. S. 287;

First Bank Stock Corp. v. Minnesota, 300 U. S. 635, 301 U. S. 234.

This judgment is final under the decisions of the state supreme court of Washington, and states "the law of the case" which is binding upon all state courts in the same proceedings.

Tucker v. Brown, 20 Wn. 2d 740, 773, 150 P. 2d 604, 622; *Davis v. Davis*, 16 Wn. 2d 607, 134 P. 2d 467; *Miller v. Sisters of St. Francis*, 5 Wn. 2d 204, 105 P. 2d 32; *Buob v. Feenaughty Machinery Co.*, 4 Wn. 2d 276, 103 P. 2d 325; *State ex rel Grays Harbor Logging Co. v. Superior Ct.*, 100 Wash. 485, 491, 171 Pac. 238, 241.

The judgment of the state supreme court fully determines all questions herein, including the federal legal questions now presented to this Court, and the same is a final appealable judgment under both the Federal and state decisions, and is clearly subject to review by writ of certiorari in this Court. A holding to the contrary would be grossly unjust, unsound, and unjustifiable.

2. SUBSTANTIAL FEDERAL QUESTIONS ARE INVOLVED.

Respondent's suggestion (p. 11) that this controversy involves only the proper method of computation of admitted taxes is wholly erroneous. The state sales tax and occu-

pation tax are entirely inapplicable to these patent royalties payable to non-residents of Washington, who are not doing business in said state, and arising out of interstate commerce transactions.

Respondent assumes, but there is no evidence which proves, that there is an "arbitrary segregation" by petitioners of the consideration payable. The selling price of these machines covered the cost of manufacture, and Lindeman's profit, plus petitioners' profit on the selling price. A patentee has a lawful right to make an additional charge of royalties for the use of patented machinery. That was all that was done here. This is not a mere matter of form, but relates to the fundamental substance of these transactions.

Any question of abuse can be met in the future when such case arises. Certainly it cannot be reasonably contended that there was any abuse, bad faith, or unlawful tax evasion in this instance. The testimony establishing the good faith of petitioners is clear, positive, and undisputed. (R. 23).

Under the state statute, quoted at page 41 of our opening brief, the ¼% business and occupation tax, if applicable, is payable by the seller or manufacturer. Petitioners have never understood or construed any of their contracts to mean that the purchasers were liable therefor, contrary to the express terms of the state statute.

And as to the 3% sales tax, this has never been collected as to the patent royalties by petitioners from any of the machine users. We must therefore assume that the loss, if any, must fall on petitioners.

As hereinabove stated, these are not "admittedly applicable state statutes." As to royalties, the statutes are not applicable at all.

Each of the four questions involved here is undoubtedly a substantial federal question.

3. INTERSTATE COMMERCE.

The admitted facts that the machines were manufactured in Washington and the purchasers resided there are in no way controlling. These were undoubtedly interstate sales and interstate commerce transactions, in view of the undisputed facts that: (1) every sales and license contract was executed by petitioners in California at their sole office at Sacramento, (R. 20-1, 44, 86, 93); and (2) substantial parts (over 15%) of the machines were manufactured by petitioners at their Sacramento plant and shipped from California to the Lindeman plant at Yakima, Washington, where they became component parts of the finished machines. (R. 14-6, 29, 33, 36-7, 39-42, 47, 88, 91-2).

Each of the cases cited by respondent (p. 14-15), sev-

eral of which were only short *per curiam* decisions, was held to involve local intrastate sales rather than interstate sales, as in each case the taxpayer was either incorporated or authorized to do business as a foreign corporation in the taxing state, had an office and numerous sales agents there, and in each case made the sale and delivery from said local office and collected payment there. These cases are therefore clearly distinguishable. They are fully distinguished in the later cases, *Freeman v. Hewit*, 329 U. S. 249, 91 L. Ed. 265, and *McLeod v. Dilworth Co.*, 322 U. S. 327, 88 L. Ed. 1304.

As the instant case involves a ¼% business and occupation tax and a 3% sales tax, under titles 2 and 3 of the state Revenue Act, the former being expressly required by law to be payable by the seller, and does not involve a use tax, it is superfluous for us to discuss the use tax cases cited by respondent, except to say that they involved local intrastate sales by companies having local offices in the taxing states, as in the sales cases hereinabove referred to.

The court will note that none of the cases cited by respondent relate to a tax directly and solely upon the seller in interstate sales, such as especially involved in this ¼% occupation tax. The state statute requires it to be paid by the seller.

Moreover, as to the 3% sales tax petitioners must bear

the loss, if there is any, as they have never collected the same on these patent royalties from any machine users.

We wish to emphasize that in any event this judgment should be reversed as to the ¼% business and occupation tax. This is expressly stated in the statute to be a tax on the privilege of doing the (interstate) business. This same Washington tax statute has been three times held unconstitutional by this Court under the Commerce Clause in cases involving interstate sales of the same nature. *Respondent has not cited a single case involving a tax of this nature.* A denial of this writ cannot be reconciled with the Fisher, Puget Sound, and Gwinn decisions of this Court.

If taxable in Washington, these patent royalties are taxable not only by the Federal Government, but also by California and Oregon. These interstate sales would thus be subject to the intolerable, unjust and unconstitutional burden of multiple taxation. *This is a direct unapportioned tax on the seller's gross receipts of sales in interstate commerce,* and hence is clearly unconstitutional.

See also the decision of this Court filed since the preparation of our petition, in *Hood v. DuMond,* U. S. 93 L. Ed. (Adv. Op.) 682, decided April 4, 1949, reversing the New York state court and holding the state statute as applied is an unconstitutional restriction on interstate commerce.

4. TAXABILITY OF PATENT ROYALTIES.

Respondent seeks to distinguish *Newport Co. v. Wisconsin Tax Commission,* 219 Wis. 293, 261 N. W. 884, 100 A.L.R. 1204, cert. denied, 297 U. S. 720, 80 L. Ed. 1004, on the ground that there the company sold patent rights, whereas here petitioners sold patented machines. This, however, is an attempted distinction without a difference. These patent royalties constitute income derived solely from certain *intangible* property, namely, patents issued by the United States Government. To tax petitioners thereon outside of the state of their domicile, California, is to deprive them of property without due process of law in violation of the Fourteenth Amendment. It was directly so held in the Newport case and other authorities therein cited.

The contract provision as to minimum patent royalties is:

> "In any event, the minimum royalty payable hereunder shall be Five Hundred Dollars ($500) per machine per annum . . . *provided, that if it shall be impossible, in the fair and reasonable judgment of Party of the First Part (Thys) to use any such machine during any part of a particular picking season because of a serious breakdown or breakdowns of a machine,* occurring notwithstanding the exercise of reasonable care on the part of the user or users thereof, *an equitable adjustment shall be made of the amount of minimum royalty payable on such machine for such picking season, based upon the number of days during which such machine*

cannot be used bears to the total number of days in the normal picking season." (Pltf. Ex. 8; R. 17, 18).

The agreement in this respect is conditional and contingent and is not definite or certain. In case of serious breakdown of a machine, not even the minimum royalty is payable.

Why should petitioners be required to pay federal income tax, in addition to California state taxes, upon the entire royalties as taxable income, and also be required to pay state sales tax and occupation tax to the State of Washington on the theory that the same is not income but is part of the gross selling price of the machines? The two are utterly contradictory. This conflict and multiple taxation can be avoided only by a decision of this Court.

The evidence is undisputed that in each instance the purchase price was fully paid and title to the machine passed to the purchaser either prior to or at the time of delivery. Each contract so provided. Other than the suspicion of counsel, there is no evidence whatever indicating any bad faith or fraudulent intent to evade taxes. The evidence is undisputed as to petitioners' entire good faith in these transactions. (R. 21-23, 44, 98; Pltf. Ex. 8).

Respondent has emphasized certain portions of the state supreme court decision referring to the $500.00 annual minimum royalty per machine. Numerous other portions

of the majority opinion, however, indicate that said decision was intended to apply to all royalties, rather than merely the minimum royalties. (R. 121, 125, 129-130).

> *If respondent is right, it would be impossible to know the amount of the selling price at the time of the sale. No one knows then what the machine will do in future years.*

5. NOT DOING BUSINESS IN WASHINGTON.

Respondent makes the surprising contention that petitioners have conceded they are doing business in Washington and conceded their liability for these taxes, but are disputing only the amount. Nothing could be more erroneous. The mere fact that petitioners are not herein presenting any question as to the tax on the cost and profit of manufacturing and the original selling price certainly does not mean that petitioners concede liability for any tax whatever on these patent royalties.

The manufacture of the machines was carried on by Lindeman Power Equipment Company, which was clearly an independent contractor, over whose operations petitioners had no control or right of control whatever. This conclusion is not altered by the fact that petitioners made certain financial loans and advances to assist Lindeman in financing its operations. That was the sole function of the bank account maintained in Washington, from which *with-*

drawals could be and were made from time to time by Lindeman.

The Yakima bank account was clearly a mere matter of practical convenience in financing Lindeman in manufacturing the machines.. (R. 37, 49). In effect these were loans made by petitioners to Lindeman to finance its manufacturing operations. (R. 87). Lindeman admitted that it commingled the proceeds of this bank account with its own funds. They were at all times treated as one and the same. (R. 90).

The machines were delivered to the purchasers as soon as completed. Petitioners never at any time owned any completed machines, parts, or stock of merchandise in this state. Clearly petitioners were not doing business in the State of Washington. See *U. S. v. American Bell Telephone Co.*, 29 Fed. 17, and the cases cited at pages 37 and 38 of our opening brief.

This conclusion is not altered by the fact that William Gamache, a large scale hop producer, to whom petitioners owed a debt of gratitude because he first successfully used these machines in this state, was paid for making arrangements with a local attorney to collect royalties and forward the same to petitioners in California. Collection of such indebtedness, it is well settled, does not constitute doing business in Washington.

20 C. J. S. 51, 52, sec. 1835, 1836, and cases cited; *14A C. J.* 1278, sec. 3984; *17 Fletcher Cyc. Corp.* (perm. ed.) 542, sec. 8492, and cases cited; *Bruner v. Moline Plow Co.*, (CCA) 168 Fed. 218; *Wagner v. Meakin*, (CCA) 92 Fed. 76.

Petitioners were therefore clearly not doing business in the State of Washington and are not lawfully subject to these claimed taxes.

CONCLUSION

We therefore respectfully submit that there is no merit in any of respondent's contentions, that the state court judgment is final and appealable, that numerous substantial federal questions are involved, that this petition for rehearing and petition for the writ of certiorari should be granted and the judgment should be reversed.

Respectfully submitted,

ELWOOD HUTCHESON
GEORGE W. WILKINS
Attorneys for Petitioners

CERTIFICATE

The undersigned attorneys for petitioners herein hereby certify that the foregoing petition for rehearing is presented in good faith and not for delay, and that the same is restricted to other substantial grounds available to petitioners although not previously presented.

ELWOOD HUTCHESON
GEORGE W. WILKINS
Attorneys for Petitioners